

In the Matter of	)	
	)	
Schools and Libraries Universal Service	)	CC Docket No. 02-6
Support Mechanism	)	
	)	

**COMMENTS OF CISCO SYSTEMS, INC.**

Cisco Systems, Inc. (“Cisco”) submits these comments in response to the Commission’s *Public Notice* seeking comment on the draft Eligible Services List (ESL) for the E-rate program for funding year 2012.<sup>1</sup> Cisco applauds the Commission’s efforts to use the ESL to provide additional clarity regarding the requirements of the E-rate program, which is essential to achieving the Commission’s goal of “simplifying and streamlining” the E-rate process.<sup>2</sup>

<sup>1</sup> Public Notice, *Wireline Competition Bureau Seeks Comment on Draft Eligible Services List for Schools and Libraries Universal Service Program*, DA 11-1096 (June 24, 2011) (“Public Notice”).

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of networks and to providing schools and libraries with a cost-effective tool to maintaining those networks.

However, the draft ESL does not adequately explain how a contract for BMIC that includes both eligible and ineligible services should be cost allocated. Earlier this year, the Commission directed the Universal Service Administrative Company (“USAC”) to approve applications for support of eligible basic maintenance services even when the same contract includes both eligible and ineligible services, provided that an applicant is “able to isolate and accurately identify the costs of the eligible services.”<sup>3</sup> However, neither the Commission nor USAC has provided adequate guidance to the industry regarding how this cost allocation should be accomplished. Accordingly, the Commission should modify its draft ESL to explain the cost allocation process for a contract that includes both eligible and ineligible basic maintenance services. Alternatively, the Commission should direct USAC to promptly amend its guidance document on cost allocation to include specific examples of BMIC cost allocation.

Likewise, the Commission should modify the draft ESL to incorporate the clarification provided by the Wireline Competition Bureau late last year regarding the scope of the Commission’s determination in the *Sixth Report and Order* that requests for BMIC would be funded only for actual work performed or for hours of labor actually

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<sup>3</sup> *Requests for Review of Decisions of the Universal Service Administrator by Chicago Public Schools, Chicago, Illinois; Coosa County School District, Rockford, Alabama; Gallup-McKinley County Public Schools, Gallup, New Mexico; Holyoke School District, Holyoke, Massachusetts; KIPP Academy, Houston, Texas; Whitley County School System, Williamsburg, Kentucky; Schools and Libraries Universal Service, Support Mechanism, Order, 26 FCC Rcd 4114, ¶ 10 (2011) (“Requests for Review Order”).*

used.<sup>4</sup> The ESL for funding year 2012 should be consistent with and accurately reflect the *Clarification Order*, which is currently not the case.

The changes to the draft ESL requested by Cisco are modest in scope but would provide important guidance to the industry in attempting to comply with the Commission's and the Bureau's recent orders regarding BMIC. These changes would benefit service providers and beneficiaries alike, and the Commission should modify the draft ESL accordingly.

## **II. THE COMMISSION CORRECTLY DETERMINED THAT BASIC MAINTENANCE SERVICES ARE ELIGIBLE FOR E-RATE FUNDING AS PRIORITY TWO INTERNAL CONNECTIONS SERVICE.**

The draft ESL reflects the Commission's determination that BMIC should continue to be eligible for E-rate funding as priority two internal connections service – a determination with which Cisco strongly agrees. Continued support of basic maintenance for internal connections is consistent with and promotes the goals of the E-rate program.

In modern computer networks, internal connections are complex systems consisting of both hardware and software. Software, consisting of millions of lines of code, is improved over time, as bugs and defects are detected in operating systems. In addition, users require on-demand technical support, particularly as networks provide greater and increasingly complicated capabilities. Cisco is able to provide all enterprise customers with access to software, tools, and information they need to maintain their networks. Online technical support and software downloads to add new functionality and security features are most efficiently shared across the global enterprise customer base.

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<sup>4</sup> *Schools and Libraries Universal Service Support Mechanism; A National Broadband Plan For Our Future*, DA 10-2355, Order (rel. Dec. 15, 2010) (“*Clarification Order*”).

In Cisco's experience, schools do not have the financial or technical resources to maintain their internal connections, and in particular software. If basic maintenance is not supported, internal connections will not receive the same basic software maintenance that enables enterprise networks, and even home networks, to function properly. Basic maintenance agreements ensure that these software modifications are properly provided to, and installed by, school networks. Furthermore, a properly designed basic maintenance agreement lowers a school's operating costs.<sup>5</sup> It would hardly benefit the country's educational system or the E-rate program to fund internal connections for schools under a framework that deprives them of the resources to maintain those connections.

While the draft ESL accurately reflects that BMIC is eligible for E-rate funding, the Commission and the Bureau recently issued decisions regarding basic maintenance services that are not adequately addressed in the draft ESL. As explained below, the Commission should modify the ESL consistent with those decisions in order to provide clarity to the industry.

### **III. THE ESL SHOULD EXPLAIN HOW A CONTRACT FOR BMIC THAT INCLUDES BOTH ELIGIBLE AND INELIGIBLE SERVICES SHOULD BE COST ALLOCATED.**

In the *Requests for Review Order*, the Commission granted waivers of funding year 2011 rules to allow applicants to cost allocate ineligible basic maintenance expenses, finding that "it is generally feasible for USAC reviewers to distinguish between eligible and ineligible services when both are included in one contract for basic maintenance

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<sup>5</sup> Operating costs are reduced in several ways, including increasing IT staff productivity by making it easier to maintain networks through the use of online tools, and lowering the costs associated with network downtime/

services.”<sup>6</sup> Accordingly, the Commission concluded “that it is no longer in the public interest to deny funding for all elements of a contract for basic maintenance services if even one element of the contract is ineligible for support.”<sup>7</sup>

The Commission made clear its preference for the cost allocation of contracts with both eligible and ineligible services, directing USAC on a going forward basis:

to approve applications for support for eligible basic maintenance services even when the eligible basic maintenance services are included in the same contract as ineligible maintenance services, as long as applicants are able to isolate and accurately identify the costs of the eligible services. This ruling shall apply beginning in funding year 2011 for applications and immediately for all pending appeals. If, however, applicants are unable to separate the eligible and ineligible services in a basic maintenance contract, USAC should deny funding for the entire contract. Nevertheless, we recommend to applicants that they attempt to avoid any potential problems or delay in the processing of their applications by entering into contracts that only include eligible basic maintenance services. Applicants ultimately bear the responsibility for demonstrating that support is requested only for eligible services.<sup>8</sup>

In the draft ESL, the Commission has indicated that “[f]unding will be provided for the eligible portion of a technical support contract that includes services that exceed BMIC, if the ineligible portion of the contract can be cost allocated. Technical support contracts that cannot be cost allocated to remove costs that are beyond BMIC, are ineligible in their entirety.”<sup>9</sup> Furthermore, according to the draft ESL, “Any cost

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<sup>6</sup> 26 FCC Rcd 4114, ¶ 9.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*, ¶ 10.

<sup>9</sup> Draft ESL, at p.23.

allocation must be based on tangible information that provides a reasonable and appropriate delineation between the eligible and ineligible components.”<sup>10</sup>

Unfortunately, neither the draft ESL nor the USAC website to which parties are directed for “additional guidance” regarding cost allocation provides any information about the appropriate methodology to allocate the cost of a contract with both eligible and ineligible services. Indeed, none of the seven cost allocation examples provided by USAC even involves basic maintenance services.<sup>11</sup>

Cisco agrees that “tangible information” and “reasonable and appropriate delineation” are reasonable and appropriate standards for assessing the cost allocation of eligible BMIC. However, these standards provide little practical guidance about how an applicant should be expected to cost allocate a contract for BMIC that contains both eligible and ineligible services.

The need for such practical guidance is particularly important given the Commission’s direction in its *Requests for Review Order* that USAC “approve applications for support for eligible basic maintenance services even when the eligible basic maintenance services are included in the same contract as ineligible maintenance services, as long as applicants are able to isolate and accurately identify the costs of the eligible services.” Such direction would ring hollow unless either the Commission or USAC explains plainly and clearly how the costs of eligible services in a contract for basic maintenance services should be isolated and identified accurately.

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<sup>10</sup> *Id.* At 28. Earlier versions of the ESL did not call for “tangible information” and asked only for a “fair” allocation of cost.

<sup>11</sup> See <http://www.usac.org/sl/applicants/step06/cost-allocation-guidelines-products-services.aspx>

Under the circumstances, either the ESL or USAC's guidelines should be modified to include a BMIC cost allocation example. For instance, tangible evidence of a cost allocation in such a case could include evidence of the existence of a "wholly eligible" actual market offer compared to an actual market offer that contains both eligible and ineligible BMIC. Such evidence should be sufficient to support a finding that an applicant has met its burden of proof.

The need for explicit guidance on the issue of allocating costs of a contract with both eligible and ineligible BMIC services is particularly important to Cisco, given USAC's decision to declare earlier this year that Cisco's SMARTnet offering is ineligible for E-rate funding. *See* USAC New Brief, *Basic Maintenance Clarification for FY2011 Applicants* (Jan. 27, 2011) (available at <http://www.usac.org/sl/tools/news-briefs/preview.aspx?id=344>). USAC concluded that "[a]pplicants cannot simply cost-allocate out the ineligible portion of SMARTnet because the Commission's rules do not allow applicants to receive support for services in a basic maintenance contract that contains both eligible and ineligible services." USAC's conclusion regarding SMARTnet cannot be reconciled with the Commission's *Requests for Review Order*, although to date USAC has not rescinded its now superseded guidance regarding SMARTnet, which only further confuses the industry. The draft ESL provides the Commission with a critical opportunity to set the record straight regarding SMARTnet by providing practical guidance on the issue of BMIC cost allocation.

**IV. THE ESL SHOULD INCORPORATE THE BUREAU'S CLARIFICATION REGARDING REIMBURSEMENTS FOR BMIC.**

The draft ESL (p. 23) includes the following language regarding when BMIC should be reimbursed: “Reimbursements for BMIC will be paid for the actual work performed under the agreement or contract.” This language is consistent with the literal terms of the *Sixth Report and Order* (§§ 106-107). However, this language is not consistent with the Bureau’s subsequent *Clarification Order* which clarified that certain types of BMIC services *do not* require a demonstration that work was performed prior to reimbursement and which made clear that these types of basic maintenance services are reimbursable as a one-time charge any time during the funding year.

Specifically, in the *Clarification Order*, the Bureau stated that: (i) “Services such as software upgrades and patches, including bug fixes and security patches, and online and telephone-based technical assistance and tools that are typically standard fixed priced offerings will continue to be funded as BMIC...”; (ii) “... reimbursement for these repairs will be permitted without demonstration of work performed...”; and (iii) “Therefore, applicants will be allowed to seek reimbursement of a one-time charge for these services at any time during the funding year.”<sup>12</sup>

Consistent with the *Clarification Order*, the ESL should be modified to distinguish explicitly between the two types of reimbursement allowable for BMIC; those BMIC services that do not require a demonstration of actual work performed and those BMIC services that do require a demonstration of actual work performed. This modification would correctly recognize that the maintenance of internal connections is

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<sup>12</sup> *Clarification Order*, § 6. The Bureau also “....explicitly distinguished these types of services from the physical maintenance and repair of equipment, such as the labor and parts needed to repair equipment at the school or library, which,...requires that work be performed before reimbursement an occur.” *Id.*



both a matter of physical repair which the Commission intended to capture in its articulation of the “actual work performed” standard, but also of continually tending to software and providing technical assistance to make sure that networks remain continuously operable. As the Bureau implicitly recognized, the modification reflects current industry practice to have all enterprise customers share the cost of software upgrades and bug fixes, as well as technical support (on line and live), since those costs are not incurred on behalf of a single customer. Indeed, those costs are incurred to help all customers of a given product or solution, globally.<sup>13</sup> Under the circumstances, Cisco recommends that the ESL for FY12 be revised to reflect that reimbursements for BMIC services will be paid: (i) annually, as a one-time charge for BMIC services such as software upgrades and patches, including bug-fixes and security patches, and online and telephone-based technical assistance without demonstration of work performed; and (ii) for the actual repairs performed for BMIC services related to the physical maintenance and repair of equipment, such as the labor and parts needed to repair equipment at the school or library.

## **V. CONCLUSION**

For the foregoing reasons, the Commission should modify the ESL as set forth above.

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<sup>13</sup> As Cisco has noted previously, the FCC’s approach to unbundled warranties is inconsistent with industry practice regarding maintenance contracts. Contracts for maintenance are standard in the IT industry and are used globally for IT networks. Revenue from these contracts funds manufacturer activities such as the development of software patches and bug fixes, which benefit all purchasers of a particular piece of equipment, as well as the funding of customer support platforms that benefit all customers. While this ESL proceeding is not a vehicle to revisit that issue, nothing in Cisco’s comment should be construed to indicate Cisco’s agreement with the current prohibition on the use of E-rate funds for unbundled warranties.

Respectfully submitted,

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